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TAX APPORTIONMENT

Recent Decisions Indicate a Review of Tax Apportionment Clauses

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As recent cases indicate, if the tax apportionment clause is not consistent with the client's intent and with sound tax principles, it can become the most significant (yet unintended) dispositive provision in the client's estate plan.

Recent decisions, such as *Estate of Lurie* **1** and *Estate of Green,* **2** continue to highlight the importance that tax apportionment clauses play in an estate plan as well as the ongoing need for a consistent review of these clauses, which are typically found amid the "boilerplate" provisions. Although boilerplate provisions *usually* do not require modification on a plan-by-plan basis, recent cases confirm that the tax apportionment clause should be viewed as anything but boilerplate. These decisions emphasize the need to analyze how your current tax apportionment clause affects your client's objectives and asset composition on a plan-by-plan basis. This article examines the tax apportionment pitfalls identified in recent decisions and discusses drafting considerations that can compensate for otherwise unanticipated results. A good introduction to the importance and effect of a tax apportionment clause is found in *Estate of Lurie.*

Shifting the tax burden

The tax apportionment clause dictates which beneficiaries will bear the burden of the estate tax. For example, should the recipient of property bear his or her share of the tax, or should the tax be paid from the residue, thereby allocating the tax to the residuary beneficiaries? Depending on the client's objectives regarding where the tax should be apportioned, the allocation of the tax burden can carry as much importance as the dispositive provisions, especially if tax ultimately is apportioned to beneficiaries whom the client did not intend to burden. **3** *Lurie* provides an interesting introduction to this topic because of the particularly harsh results that can occur when tax is apportioned to a marital share that does not give rise to any tax but instead provides a tax deduction.

In *Lurie*, the tax apportionment clause in the decedent's revocable trust agreement directed the *trustee* to pay all taxes; this provision essentially directed that the taxes be paid from the residue rather than from the specific assets generating the tax. This drafting approach is referred to as an anti-apportionment clause because rather than specifically apportioning tax to the sources that generate the tax, the residue of the estate is responsible for the tax burden. The trust in *Lurie* also provided that to the extent there were not enough assets in the probate estate to pay the estate tax, that tax was to be paid from the revocable trust. The tax apportionment clause *Lurie* provided as follows:

> 4.1 Debts and Taxes. Upon the death of the Grantor, the Trustee shall, to the extent that the assets of the Grantor's estate * * * are insufficient, pay * * * reasonable expenses of administration of his estate, * * * all income, estate, inheritance, transfer and succession taxes, including any interest and penalties thereon, which may be assessed by reason of the Grantor's death, without reimbursement from the Grantor's Executor or Administrator, from any beneficiary of insurance upon the Grantor's life, or from any other person; . . . .

Unfortunately, such a clause was not the preferable choice for the *Lurie* estate. Because of the asset composition of the estate, the trust residue was not large enough to cover the tax generated on assets that were included in the taxable estate but were not part of the residue. In *Lurie*, after the estate filed the estate tax return, the Service issued a notice of deficiency, which included in the gross estate the value of additional trusts over which the decedent presumably held an interest. These additional trusts, called "notice trusts" in the opinion because they were identified in the notice of deficiency, increased the taxable estate, but did not provide the trustee with access to principal nor did they provide the trustee with the ability to seek reimbursement for taxes.

Because the tax apportionment clause directed that all tax was to be paid "without reimbursement . . . from any other person," the residue was responsible for the increased estate tax and no part of the tax generated by the additional notice trusts could be recovered from those trusts. **4** The burden on the residue forced a reduction in the marital trust to satisfy the tax burden, but as the marital deduction decreased, the overall tax increased, creating a tax-on-tax phenomenon.

In hindsight, it would have been more tax-efficient to apportion the tax to (i.e., seek reimbursement from) the entities or assets causing the tax. Despite the adverse result in *Lurie*, the type of clause used there is common and can be helpful-for example, where the client wants to preserve the principal in an asset or bequest, rather than depleting a bequest or reducing a separate taxable trust by payment of the tax from the trust's principal. The lesson to learn from *Lurie* is that the tax apportionment clause should be considered as important as a dispositive clause, because under certain circumstances, the outcome can be as influential on the client's intent as the dispositive clauses.

Impact of equitable apportionment and the tax apportionment clause

The result in *Lurie* highlights the purpose of drafting and including in a will (or a will and trust) a tax apportionment clause that is intended to circumvent the application of an equitable apportionment statute under local law. **5** While **IRC Section 2002** imposes on the executor the responsibility of paying the federal estate tax, how that tax is allocated among the beneficiaries of the estate is determined either by the governing instrument, or pursuant to state law. **6** Absent a clearly expressed intent under the governing instrument, most courts will apply judicial construction. If the testator's intent cannot be determined through judicial construction, a court will apply state statutory law or common law, both of which are usually based on the doctrine of equitable apportionment.

Many states adopt the doctrine of equitable apportionment, which generally holds that the burden of taxes is imposed on the property that generates the tax. For example, suppose that an estate plan is unclear as to who bears the burden of the tax, and both a charitable and non-charitable beneficiary share the residue. Under the doctrine of equitable apportionment, none of the tax burden would be allocated to the charity because the charitable portion does not generate any of the estate tax. Similarly, if distribution to all the beneficiaries generates a tax, that tax will be apportioned among all the beneficiaries in proportion to the value of the property received.

Although state laws differ, many states adopt some form of equitable apportionment rather than apportioning the tax burden on the residue. An emerging trend in many states has been the adoption of the Uniform Estate Tax Apportionment Act (the "Uniform Act"). **7** The Uniform Act was initially drafted in 1958, but has been amended and revised numerous times-most recently in 2003. Consistent with the concept of equitable apportionment, the Uniform Act directs that estate tax be apportioned to the gross estate reduced by (1) claims or expenses allowable as a deduction, (2) property that qualifies for a marital or charitable deduction or is otherwise deductible or is exempt, and (3) any amount added to the gross estate because of a gift tax on transfers made before death. **8**

The comments to the Uniform Act indicate that "a decedent's direction will not control the apportionment of taxes unless it explicitly refers to the payment of an estate tax and is specific and unambiguous as to the direction it makes for that payment." **9** Most notably, the Uniform Act provides relief for a trustee who, while forced to pay an estate tax on property passing to beneficiaries, is unable to access the underlying funds to pay the tax (i.e., the *Lurie* situation). **10**

It is important to recognize how a state's apportionment law may apply and to ensure that both the will and trust are coordinated to direct the desired outcome. **11** Generally, there are two alternative methods to express the client's intent in apportioning the tax: (1) a pro rata apportionment based on receipt of property among legatees, devisees and residuary beneficiaries of the estate, allocated in relation to the property received (i.e., equitable apportionment), or alternatively, (2) an anti-apportionment formula that allocates the tax payment only to the residue and therefore to the residuary beneficiaries-not the legatees or devisees. A properly drawn tax clause will clearly reflect one of these alternatives. For example, if the tax is to be allocated to the residue as it was in *Lurie*, the tax clause should specifically direct that the executor or trustee shall pay all taxes from the residue "without apportionment" in order to ensure that the intent is clear. **12**

At a minimum, the anti-apportionment clause should also allow a trustee to access funds included in the gross estate and incurring estate tax but passing outside the estate. Such language could be added to the end of a *Lurie*-type clause and could read as follows: "except that the amount, if any, by which the estate and inheritance taxes shall be incurred as a result of the inclusion of property in which the grantor has a qualifying income interest for life, over which the grantor may have a power of appointment, or that is not held as a part of or payable to the grantor's estate or trust following the grantor's death, shall be paid by the person holding or receiving that property." If such a clause had been used in *Lurie*, it would have alleviated the problem.

A lesson on testator's intent

The issue of the testator's intent regarding the tax apportionment clause was the subject of litigation in the estate of former television personality Charles Kuralt. **13** The estate argued that there was an ambiguity surrounding the intent of the will and the tax apportionment clause, but the Montana Supreme Court held that the tax apportionment clause did in fact clearly direct the payment of taxes from the residue of the estate.

The alleged ambiguity arose from a codicil that was in the form of a handwritten letter that the decedent executed in 1994, devising his Montana ranch to his "long-time and intimate companion." **14** The residuary beneficiaries (who included his surviving spouse and two daughters but did not include the companion) argued that the later-executed holographic codicil (the letter) "created adverse tax consequences against the estate, contrary to the 'dominant purpose or plan of distribution' of the 1994 will," which was "to take full advantage of the marital deduction and to protect Mrs. Kuralt from burdensome taxation." **15** The tax apportionment clause directed taxes to be paid from the residue, and therefore the tax on the devise of the Montana real estate was satisfied from the residue rather than directly against the real estate, thereby creating more tax. **16**

The estate argued unsuccessfully that the "holographic codicil renders ambiguous the otherwise clear language of the will, and that, in light of this ambiguity, there exists a conflict between the dominant purpose of the will and the anti-apportionment language." **17** In the absence of clear intent, the estate argued that applicable state (New York) law should be applied, which would have allocated the tax burden among the legatees and devisees (including the companion) in proportion to their interest received, (unless directed otherwise under the will). **18**

The court, however, determined that the will provided clear and unambiguous intent, directing the payment of tax from the residue under the anti-apportionment clause, which negated the need for the court to look to local law. Therefore, based on the clear intent of the testator regarding the tax apportionment clause, the court found that none of the tax burden was apportioned to the companion and instead the full tax burden was allocated to the residue. **19**

Tax allocated to charity

Estate of Green involved the tax-on-tax phenomenon previously noted in *Lurie*, as well as the contention in *Kuralt* regarding the clarity of the testator's intent. Specifically in *Green*, an unclear tax apportionment clause resulted in all of the generation-skipping transfer ("GST") tax being allocated against the share of the residue passing to charity. Generally, most practitioners would agree that it is preferable not to allocate any tax to charitable beneficiaries. This is particularly relevant with respect to GST tax, because as can be seen in *Green*, each dollar of GST tax allocated to charity reduced the charitable deduction. This, in turn, increased the tax, which further reduced the charitable deduction, resulting in the tax-on-tax phenomenon.

In *Green*, the decedent divided her residuary estate between a charitable foundation and her grandchildren. The transfer in trust for the grandchildren constituted a direct skip, subject to both estate tax and GST tax, and the transfer to the foundation qualified for the charitable deduction. At issue was whether the decedent's will apportioned the tax. The will directed the personal representative to pay from the estate all estate and death taxes. However, although such language is a general direction found in many documents, it did not address tax apportionment within the residue.

The decedent did not provide any other direction regarding tax apportionment other than to expressly direct that the payment of GST taxes should not be "charged against nor deducted from" any property passing to skip persons. This is a fairly common exclusion because to accomplish a GST transfer without reducing the property to pay the GST tax, the estate plan must override the express language of **Section 2603** . **Section 2603(b)** provides that unless the estate plan directs otherwise by specific reference to the payment of GST tax, the tax is charged against the property constituting the transfer. Thus, while the Tax Court in *Green* found that the will prevented apportionment of GST tax against the GST transfer, the will did *not* direct whether estate taxes were to be apportioned between the foundation and the grandchildren.

Because the Tax Court in *Green* found a lack of clear intent as to who should ultimately bear the estate tax burden, the court applied the doctrine of equitable apportionment as applicable under state law. Under this doctrine, the court determined that because no portion of the residue passing to the foundation generated estate tax, the foundation's share of the residue was exonerated from allocation of estate tax, and accordingly the full amount of the estate tax (but not GST tax) should be apportioned to the grandchildren's share.

The tax clause was effective regarding the apportionment of the GST tax because the express language of the will overrode **Section 2603(b)** ; therefore, all the GST tax was charged against the charitable portion of the residue. The difficulty with this type of tax apportionment is that each dollar of GST tax paid from the charitable portion increased the amount of estate tax due (because of the reduction in the charitable deduction). This increased estate tax in turn reduced the grandchildren's share.

Anatomy of a tax apportionment clause

The goal of any tax apportionment clause is to express clearly the testator's intent regarding who should bear the tax. The consequences of failing to achieve this goal are illustrated in *Lurie*, *Kuralt,* and *Green.* Additionally, because of the default provisions under state law, the tax apportionment clause should be evaluated and perhaps modified to reach the desired result on a case-by-case basis. Therefore, the following roadmap considers the anatomy of a tax apportionment clause as three main components:

(1) the general payment of taxes, indicating without apportionment but establishing priorities for payment if taxes must be from certain assets,

(2) specifically apportioning tax to certain assets by providing for recovery of tax from certain assets included in the decedent's estate, and

(3) the special treatment of marital property for apportionment purposes, including the possibility of waiving the right of recovery over such property.

An initial question is whether it is adequate to use an anti-apportionment clause (as in *Lurie*) which directs that taxes be paid solely from the residue, with additional language that allows the trustee to collect taxes from property included in the gross estate but not accessible by the trustee. Alternatively, is even more direction in the clause necessary, depending on what assets comprise the residue?

For example, there are certain components, such as marital or charitable trusts, which-when included in the residue and subject to tax-produce adverse tax results if used to pay estate tax. As *Lurie* and *Green* illustrated, marital and charitable trusts should be specifically excluded from the payment of estate tax through express language. To alleviate or lessen the likelihood of these adverse tax effects, the general tax payment clause could initially direct the payment of tax without apportionment, and then could establish an ordering of priorities so that, to the greatest extent, specific assets would not bear any of the tax. For example, after directing the payment of tax without apportionment, the tax clause could identify certain types of assets that, if desired, should not be apportioned tax, including the following:

(1) Qualified plan benefits and income in respect of a decedent ("IRD") property ideally should not be

apportioned tax because when such property is liquidated to pay the tax, there is recognition for income tax purposes. Consequently, these IRD-type assets can be more tax-costly than other non-IRD assets.

(2) General legacies and specific bequests normally should not be apportioned tax because doing so may frustrate the overall intent of the testator in making such a legacy or bequest (i.e., it is likely that the testator intended the legatee to receive the gift in whole); otherwise, the executor could be forced to sell the asset to reimburse the estate for the apportioned tax.

(3) Property that qualifies for the marital deduction should not be apportioned tax because reducing the marital deduction creates a tax on a tax (as discussed earlier in connection with *Lurie*).

(4) Property that qualifies for the charitable deduction should not be apportioned tax because reducing the charitable deduction creates a tax on a tax as the deduction is reduced (as discussed in connection with *Green*).

If tax must be apportioned to the above items, it may be preferable to apportion tax to the items in the order listed above. For example, while paying tax from qualified plan benefits triggers the recognition of income tax, the overall tax increase is likely less than the tax-on-tax burden caused by reducing a marital or charitable deduction.

Alternatively, in the case of some assets, it is preferable to direct the executor or trustee to seek reimbursement directly from the source responsible for the tax. Accordingly, it is appropriate to follow the initial "without apportionment" language (or anti-apportionment language) with the proviso that the executor or trustee may recover a pro rata portion of the taxes from certain beneficiaries of property (or trusts, for example, as in *Lurie*) that are included in the decedent's estate but that pass outside the residue. Such property perhaps should be apportioned tax or the executor or trustee should seek reimbursement because the property is not held as a part of the estate, and therefore the executor or trustee cannot access payment if the residue is insufficient.

Common examples include property as to which the executor or trustee otherwise already has a right of recovery or reimbursement (such as life insurance that is includable in the estate under **Section 2042**) but which likely will pass to a designated beneficiary directly and not through the estate, and therefore the executor or trustee is allowed to apportion and recover estate tax from the beneficiary under **Section 2206** . A similar example is property includable in the estate under **Section 2041** because of a power of appointment (such as the notice trusts in *Lurie*). The executor or trustee generally should be allowed to apportion and seek reimbursement for estate tax attributable to **Section 2041** property by virtue of **Section 2207** , which allows a pro rata recovery of the taxes apportioned.

This recovery clause would have required the trustee in *Lurie* to collect from the trustees of the notice trusts each trust's pro rata share of tax liability; as a result, the marital share would not have been reduced. This treatment, however, must be consistent with the client's intent. For example, in *Lurie*, the client may have instructed the attorney to preserve the principal balance in the notice trusts regardless of the adverse impact on the marital trust.

Furthermore, while a clause providing for apportionment protects against unintended consequences of property passing outside the residue, it can and should be modified if a client expresses the intent to pass a specific asset without tax being apportioned against it. For instance, a client may have indicated that a family business or a parcel of real estate held in joint tenancy should pass to the co-owner or intended recipient without the burden of the tax assessed on the specific asset. In that circumstance, the clause should be modified to specifically exclude the family business interest or parcel of real estate from the application of the tax apportionment clause, and to shift the tax burden to the residue of the estate unless the intent was that other non-residual gifts pay their portion of the tax.

A final element of a tax apportionment provision pertains to waiver of the right of recovery provided under the Code. **Sections 2206** , **2207** , and **2207B** are part of a federal statutory equitable apportionment regime that entitles reimbursement for the proportionate share of estate tax attributable to the inclusion of property passing outside the estate (or trust). **20** These Code sections are effective unless the decedent's estate plan indicates otherwise. **21**

A tax apportionment clause might follow the treatment under **Section 2206** which grants recovery of tax for property includable under **Section 2042** , such as a life insurance policy payable to an unrelated third party. **22** However, since recovery is generally not advisable from marital or charitable property, the tax apportionment provision could include an additional sentence to waive reimbursement by directing the executor or trustee to waive the right of recovery under **Sections 2207** and **2207B** from any property included in the decedent's estate that qualifies for, or is elected to qualify for, the federal estate tax marital or charitable deduction. **23**

Separate tax apportionment for marital property

In addition to the standard tax apportionment clause, it is helpful to address separately any property that is included in a decedent's estate and that previously qualified for the marital deduction in the estate of the decedent's predeceased spouse, or in more than one predeceased spouse's estate if the client survived more than one spouse. The separate marital property tax clause should be tailored to apply only to property that qualified for the marital deduction in the predeceased spouse's estate. **24**

The general goal of a marital property tax clause is to direct the executor or trustee to collect or waive the incremental amount of tax generated by the inclusion of a marital trust (created by a predeceased spouse) in the client's estate. Where there is more than one marital trust, and one marital trust is GST tax-exempt, it may be desirable to direct the executor or trustee to collect the estate taxes attributable to the GST tax-exempt marital trust from a marital trust that is not GST tax-exempt in order to preserve the GST tax-exempt property. To accomplish this goal, the executor or trustee must expressly waive the right of recovery under **Section 2207A** , which must be done by specifically directing the executor or trustee to "waive the right of recovery under **Section 2207A** " from any marital trust property that is GST tax-exempt. This concept of waiver is discussed in greater detail below.

Waiver of recovery from marital property: The implications of Sections 2207 and 2207A

Sections 2207 and **2207A** address when and to what extent the assets of a marital trust will be used to pay estate tax. **Section 2207A** grants the estate of a surviving spouse a right of reimbursement for estate taxes assessed on property held in a QTIP marital trust which is included in the client's estate because of **Section 2044** (regarding property for which a QTIP election was made). Under **Section 2207A** , the estate is entitled to collect the *incremental* amount of tax resulting from inclusion of the property in the estate; this means that the property is deemed to be taxed at the highest marginal rate applicable to the estate.

Similarly, **Section 2207** grants the estate of a surviving spouse a right of reimbursement for estate taxes over property included in the spouse's estate under **Section 2056** due to a general power of appointment. By contrast, however, the amount of estate tax the surviving spouse's estate is allowed to collect under **Section 2207** is not an incremental amount of tax, but rather is the pro rata portion of estate tax representing the ratio that the value of the property bears to the entire taxable estate.

For GST tax purposes, an individual (or his executor) is allowed to allocate his unused GST exemption to property over which he is the transferor (for example, property subject to estate tax in his estate). **25** A marital trust is a deduction from the gross estate and so is not subject to tax in the estate of the decedent creating the trust. Accordingly, the decedent is not considered the transferor under **Section 2652** , and therefore would not be allowed to allocate his unused GST exemption to such property without an exception to the general rule. Such an exception is provided under **Section 2652** for a decedent creating a QTIP trust. Under that section, the estate of the decedent (or the donor spouse for a lifetime QTIP) can make a special election to treat the QTIP trust for GST tax purposes as though the QTIP election was not made. This "reverse QTIP election" allows the decedent's executor to allocate the decedent's unused GST exemption remaining at death to a QTIP trust. **26** Thus, the decedent creates two QTIP trusts-one that is GST tax-exempt because GST exemption has been allocated to it via the reverse QTIP election, and a second QTIP trust that is not GST tax-exempt. **27**

It is important to understand the effect of a waiver of the right of recovery when the estate tax attributable to both QTIP trusts on the death of the second spouse is paid either from the GST non-tax-exempt trust or from other assets in order to preserve the principal remaining in the GST tax-exempt trust. The marital property tax clause should (1) direct the executor or trustee holding any marital trust property (i.e., the QTIP trust) to certify to the executor or trustee of the decedent's estate the increase in the amount of estate tax caused by the inclusion of marital trust property in the estate, and (2) grant the executor or trustee of the estate the *discretion* to recover from the trustee of the marital trust property either (a) the amount certified, (b) a lesser amount, or (c) a greater amount. However, to preserve the principal in the GST tax-exempt QTIP trust, and not have the executor or trustee recover the tax, the marital property tax clause must direct the executor or trustee to waive the right of recovery granted under **Section 2207A** in order to avoid a constructive addition for GST tax purposes.

Reg. 26.2652 provides examples of the effect of a reverse QTIP election on constructive additions for GST tax purposes. The examples indicate that the failure to exercise a right of recovery is not considered a constructive addition for purposes of the GST tax. However, for gift tax purposes, the failure to exercise a right of recovery *is* treated as a transfer from the individuals who would benefit from the recovery (the beneficiaries of the estate) to the individuals from whom the recovery would have been obtained (the beneficiaries of the marital trust). **28**

There is an exception under the Regulations indicating that "to the extent the surviving spouse's will provides that a recovery shall not be made or to the extent that the beneficiaries cannot otherwise compel recovery," then the failure to exercise the right of recovery will not be treated as a gift. **29** Hence, if the executor or trustee is given the discretion to waive the right of recovery over marital trust property, the beneficiaries cannot otherwise compel recovery, and thus there is no deemed gift. There may, of course, be circumstances where the executor or trustee prefers to use the assets in the GST tax-exempt QTIP trust, such as where the remainder beneficiaries are the children from a prior marriage, and in that case, the right of recovery under **Section 2207A** would *not* be waived.

Conclusion

The purpose of the tax apportionment clause is to express clearly the testator's intent regarding who should bear the estate tax. The consequences of not fulfilling this purpose are illustrated in *Lurie* and *Green*-cases that very likely produced results inconsistent with the client's intent. Additionally, because of the default provisions under state law, the tax apportionment clause should be evaluated and perhaps modified (1) to reach the desired result on a case-by-case basis and (2) to avoid the unintended application of state law in place of an ambiguous tax clause. Although the tax apportionment clause may be surrounded by boilerplate language, its purpose is anything but boilerplate and the clause must be evaluated for each estate plan. As case law shows, if the tax apportionment clause is not consistent with the client's intent and with sound tax principles, it can become the most significant (yet unintended) dispositive provision in the client's plan.

PRACTICE NOTES

Qualified plan benefits and income in respect of a decedent (`IRD') property ideally should not be apportioned tax because when such property is liquidated to pay the tax, there is recognition for income tax purposes.

1

TC Memo 2004-19 , RIA TC Memo ¶2004-019, 87 CCH TCM 830 .

2

TC Memo 2003-348 , RIA TC Memo ¶2003-348, 86 CCH TCM 758 .

3

See, generally, Kanner, "Tax Apportionment Clauses That Carry Out a Client's Intent," 19 ETPL 150 (May/June 1992), for a review of the issues to consider when evaluating a client's intent and drafting tax apportionment clauses.

4

The estate tax return reported a gross estate of $91 million. Because the decedent had used all of his applicable exclusion amount during life, the entire estate (less $30,000 in administrative expenses) funded the marital trust. When the additional notice trusts worth $40 million were added to the gross estate, the tax apportionment clause directed that the additional estate tax on the $40 million be paid from the amount otherwise passing to the marital trust. Hence, the increase in tax reduced the marital deduction, and created a tax-on-tax situation.

5

If the estate plan in *Lurie* had been silent on the issue of tax apportionment, Illinois common law would have allocated the tax to the assets causing the tax (i.e., the notice trusts) rather than to the residue, and a lower overall tax would have resulted. See In re Estate of Gowling, 411 NE2d 266 (Ill., 1980), for a review of the Illinois common law on equitable apportionment.

6

Section 2002 imposes the liability for payment of the estate tax on the executor, and **Section 2203** provides that if there is no executor or administrator appointed, then any person in actual or constructive possession of property of the decedent will be liable for payment. This follows longstanding principles articulated in *Riggs v. Del Drago*, **29 AFTR 1205** , 317 US 95, 87 L Ed 106, 42-2 USTC ¶10219 (S.Ct., 1942), in which the Supreme Court held that Congress did not intend to override state laws regarding the devolution of property; rather, applicable state law should govern the ultimate impact of the federal estate tax upon the beneficiaries of an estate. Moreover, the Service ultimately retains recourse against the transferees of transferred estate assets under **Section 6324** , if necessary, once assets have been transferred. Refunds of tax likewise are distributed based on the same apportionment method. See In re Estate of Siebrasse, 2004 SD 46 (Sup. Ct. S.D., 4/7/04), in which the Supreme Court of South Dakota held that the local law regarding apportionment applied to the ultimate tax liability; thus, where the tax is apportioned pro rata, a subsequent refund of such tax must also be distributed pro rata in accordance with the statute.

7

See Uniform Estate Tax Apportionment Act (hereinafter the "Uniform Act") §2 of 1964, and §3-916 of the Uniform Probate Code, as revised in 2003 by the National Conference of Commissioners on Uniform State Laws, which can be accessed at www.nccusl.org. For a thorough review of the Uniform Act, see

Kahn, "The Revised Uniform Estate Tax Apportionment Act," 38 Real Prop. Prob. & Tr. J. 613 (Winter 2003).

8

Uniform Act §2.

9

Comments to Uniform Act §3; see also, Robinson, "Tax Apportionment Problems Under the Georgia Probate Code," 8 Ga. B.J. 16 (June 2003), for a general review and application to Georgia.

10

Uniform Act §8.

11

See Zaritsky, "Tax Apportionment and the Pour-Over Will," 23 ETPL 342 (Aug./Sept. 1996), for a discussion of the importance of a coordinated estate plan. In that article, the author reviews *Leavenworth Nat'l Bank*, 1996 WL 225193 (D.C. Kan., 1996), where the court reasoned that the decedent's will directed tax to be paid from the estate generally, regardless of which beneficiaries were charged pursuant to the will, while the Kansas common law (which was not applied because the will provided direction) alternatively would have spared apportioning to a marital bequest.

12

Regarding direction to the executor or trustee under the clause, if a pour-over will and a revocable trust are drafted, the tax apportionment clauses in both documents should mirror each other. Frequently one document, such as the will, will grant the trustee of the revocable trust the discretion to exercise any powers otherwise available to the executor of the will; thus, the clause will direct either the executor or the trustee, or both.

13

In re Estate of Kuralt, 68 P3d 662 (2003); see, also Volkmer, "Apportionment of Estate Tax Determined," 30 ETPL 463 (Sept. 2003), for a review of the litigation and the final decision.

14

Kuralt, 68 P.3d at 663.

15

Id. at 664.

16

Presumably by reducing the marital deduction, because as indicated in the above quote, the estate argued that the surviving spouse was unable to take full advantage of the marital deduction. The exact cause of the increased tax was not mentioned in the case or in the two lower court decisions, Kuralt I (In re Estate of Kuralt, 981 P2d 771 (Mont., 1999)), and Kuralt II (In re Estate of Kuralt, 15 P3d 931 (Mont., 2000)).

17

Kuralt, 68 P.3d at 666.

18

N.Y. Est., Powers and Trusts Law §2-1.8(c).

19

Although the estate was burdened with prolonged litigation, the litigation was driven by the estate beneficiaries in order to potentially circumvent the application of the will's tax allocation clause, thereby increasing the amount available for distribution in the residue. For a review of common litigation issues and pitfalls associated with estate plans, see Raithel, "Drafting Estate Planning Provisions to Avoid Litigation," 27 ETPL 55 (Feb. 2000).

20

Who is entitled to the recovery is not consistent in the Code: **Sections 2206** and **2207** indicate that the executor is entitled to recover and, absent an appointed executor, **Section 2203** indicates that the person in possession of property (presumably a trustee) would be entitled. On the other hand, **Sections 2207A** and **2207B** indicate that the decedent's estate is entitled to recover. See Pennell and Danforth, 834 T.M. (BNA), *Transfer Tax Payment and Apportionment*.

21

Waiver under **Sections 2206** and **2207** may be accomplished by a general waiver (i.e., the waiver does not have to specifically mention the Code section), but waiver under **Section 2207B** (and **Section 2207A**) must specifically indicate the intent to waive under that Code section. See **Sections 2207A(a)(2)** and **2207B(a)(2)** .

22

The executor or trustee is granted a right to recover the portion of the estate tax attributable to life insurance under **Section 2206** .

23

See Handler and Dunn, "Drafting the Estate Plan: Law and Forms" (Aspen Publishers 2003), for detailed sample language and commentary addressing tax apportionment generally under Form 10.

24

A topic that is beyond the scope of this article but should be mentioned here is the required modification to the tax apportionment clause if a Clayton contingent QTIP trust (a "Clayton Marital") is used. If a Clayton Marital is used, no other QTIP planning should be used. The concept of a Clayton Marital is derived from *Estate of Clayton*, **70 AFTR 2d 92-6262** , 976 F2d 1486, 92-2 USTC ¶60121 (CA-5, 1992), as later clarified in **Reg. 20.2056(b)-7(d)(3)** . When a Clayton contingent QTIP is used, the portion of the marital trust for which QTIP is not elected (the "non-elected" portion) funds the credit shelter trust, and the elected portion typically constitutes the residue. As Sebastian V. Grassi notes in his article cited below, because the non-elected portion will not be treated as a marital trust, the tax apportionment clause must be modified to "ensure that estate taxes attributable to the non-elected portion (i.e., the portion that is distributed to the credit shelter trust) are not apportioned against the residuary as a whole and thus indirectly against the QTIP marital deduction trust, which is part of the residuary." Grassi, "Tax Changes Put Premium on Drafting Flexible Estate Plans," 71 Prac. Tax Strategies 140 (Sept. 2003). See also, Grassi, "Drafting Flexibility Into Trusts Helps Cope With Uncertainty," 29 ETPL 347 (July 2002).

25

Section 2631 .

26

Section 2652 is also applicable to lifetime QTIP trusts pursuant to **Section 2523(f)** ; see also **Reg. 26.2652-2** .

27

This technique accommodates situations where the value of the marital trust exceeds an individual's remaining GST exemption available at death.

28

Reg. 20.2207A-1(a)(2) .

29

Reg. 20.2207A-1(a)(3) .